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MEMORANDUM FOR: Mr. Donald Syvrud
Deputy To Assistant Secretary
for International Affairs
Department of the Treasury

SUBJECT : Developed Countries: Economic Policy Positions

Attached is a summary of economic policy priorities in the major developed countries, per your request of 12 August. We hope that this paper will provide useful background for Secretary Simon's upcoming speech. If you have any further questions, please call [redacted] 25X1A9A or [redacted] on IDS Code [redacted] 25X1A

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Attachments:
As stated

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DEVELOPED COUNTRIES: CURRENT ECONOMIC POLICY POSITIONS

. Unemployment gradually is supplanting inflation and payments deficits as the principal concern of economic policymakers in the major foreign developed countries. So far, however, anxiety over spreading joblessness has not been translated into vigorous policy action. Most countries continue to grope for an economic strategy that will be effective in combating the slump yet will not jeopardize gains made in controlling inflation and reducing payments deficits.

By any measure, the global slump has taken a painful toll on workers' jobs. West Germany, France, and Britain all are experiencing their worst unemployment in the postwar era. The jobless rate in Japan is the worst in twenty years; in Canada it is at a fourteen year high. Italian figures, which show only a small rise in unemployment, mask a substantial amount of hidden unemployment in the form of short-time work. With all signs pointing toward a tardy and slow recovery, the developed countries, particularly the European countries, face the prospect of rising unemployment through the end of 1975.

CAUTIOUS REFLATION

Of the six major foreign industrialized countries, only Italy has thrown caution to the wind and embarked on a vigorous program of domestic reflation. In recent weeks, Rome has announced a $5.5 billion (3% of GNP) program of fiscal expansion; it has

been encouraging an expansionary monetary policy since early in the year. Japan has gradually reflated since the first of the year and plans to go further this fall, while Canada is trying to follow neutral policy course. Germany and France have vocally supported the need for reflation, but the measures they plan for later in the year are relatively mild. Bonn's scheduled $2 billion expansion of public investment will do little more than offset anticipated cutbacks in other sectors. The planned French program of $3.5 billion is quite moderate given the depth of the recession in France.

THE INFLATION CONSTRINT

The unbridled inflation of recent years has left a legacy of caution among most policymakers that continues to moderate all steps toward reflation.

Inflation is still the main preoccupation of policymakers in Canada and Britain. Ottawa is maintaining a fairly neutral policy position, hoping that inflation will abate before it sets out to reduce the country's high unemployment rate. London has only recently embarked on an anti-inflation program and, with the worst inflation in the developed world, will be in no position to adopt expansionary policies in the next six months, even though the government will be under increasing pressure from the labor unions to hold down unemployment.

Inflation is less of a policy constraint in France, Germany, Japan, and to some extent Italy, which have all made considerable

progress in reducing price increases. Even though governments in these countries would prefer even more evidence that inflation has been truly harnessed, they generally believe that expansion poses only a moderate risk of rekindling inflation since output is running well below capacity.

THE PAYMENTS CONSTRAINT

At the present time, the foreign sector is probably the most important constraint on policy actions to spur recovery. In the last year, Japan, France, Britain and Italy have all made remarkable progress in reducing their payments deficits. These gains, however, are considered highly fragile, the transitory product of steep recession. Each country worries that if it expands more rapidly than its trading partners, its imports will swell without any corresponding rise in exports, thus leading to a renewal of unmanageable payments deficits.

France and Japan appear to place the highest priority on maintaining a strong payments position. Tokyo's reluctance to let the economy recover at a rate much faster than that of the United States, its major trading partner, is moderating the pace of reflation in Japan. French orthodoxy abhors a payments deficit, and Paris is tilting its expansionary policy in the direction that poses the least threat to its recently strengthened current account.

Besides worrying about renewed deficits, policymakers, especially in Germany, feel that the sharp decline in world trade

has rendered domestic expansionary policies less effective. Shrinkage in exports accounts for a large part of the decline in economic activity in the Six since the first of the year. Stimulating domestic demand would do little to help the hard-hit export sector, and each country is adamant than a strong export sector is vital.

Until recently, the major European countries have been content to sit tight, awaiting a pickup in world demand. With few signs of an upturn on the horizon, the wait for export-led growth has become ever more frustrating. France and Germany now are finding mounting support for their view that the stronger economies must adopt a policy of coordinated reflation.

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